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Collections and refunds of taxes

Washington

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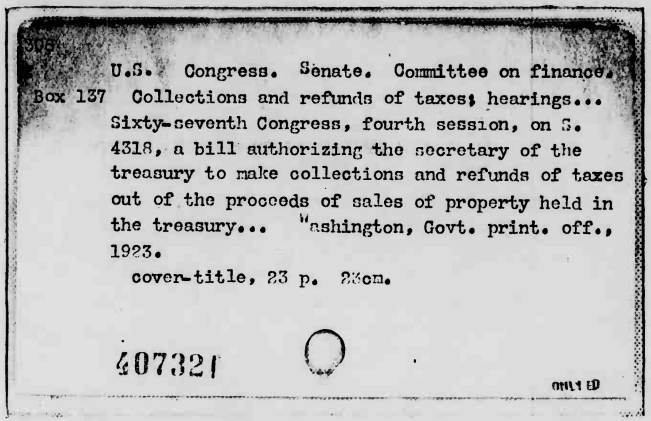

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COLLECTIONS AND REFUNDS OF TAXES

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HEARINGS

BEFORE THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

SIXTY-SEVENTH CONGRESS
FOURTH SESSION

ON

S. 4318

A BILL AUTHORIZING THE SECRETARY OF THE TREASURY TO MAKE COLLECTIONS AND REFUNDS OF TAXES OUT OF THE PROCEEDS OF SALES OF PROPERTY HELD IN THE TREASURY

Printed for the use of the Committee on Finance.

WASHINGTON
GOVERNMENT PRINTING OFFICE
3443 1923

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COLLECTIONS AND REFUNDS OF TAXES.

THURSDAY, JANUARY 25, 1923.

UNITED STATES SENATE,
COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to call, at 10.30 o'clock a. m., in room 310, Senate Office Building, Hon. Porter J. McCumber, presiding.

Present: Senators McCumber (chairman), Smoot, McLean, Calder, Williams, Jones, and Gerry.

The committee thereupon proceeded to the consideration of S. 4318, a bill authorizing the Secretary of the Treasury to make collections and refunds of taxes out of the proceeds of sales of property held in the Treasury.

The CHAIRMAN. Senators, we have up for consideration this morning Senate bill 4318, which reads as follows:

[S. 4318, Sixty-seventh Congress, Fourth Session.]

A BILL Authorizing the Secretary of the Treasury to make collections and refunds of taxes out of the proceeds of sales of property held in the Treasury.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That in case income has been received by any person who was or subsequently became an alien enemy or by any corporation the majority of whose shares of outstanding stock was owned by persons who were or subsequently became enemy aliens and such person or corporation has failed to pay any taxes payable under any revenue act of the United States, or such taxes have been paid by citizens of the United States or by such corporations after the majority of its outstanding shares of stock has been purchased from the United States or from some officer or official of the United States by citizens of the United States or by a domestic corporation all of whose outstanding shares of stock were owned by citizens of the United States, the Secretary of the Treasury is authorized and directed to collect such taxes out of the proceeds of the sale of such shares of stock or other property of such person or corporation which has been deposited in the Treasury of the United States pursuant to law and to make refundment to such citizens of the United States or to such corporation of all taxes so paid by them and charge the amount so refunded against the proceeds of the sale of such shares of stock or such other property so deposited in the Treasury of the United States.

The CHAIRMAN. I believe that Mr. Appel is here and wants to be heard. What is your name?

STATEMENT OF MR. MONTE APPEL.

Mr. APPEL. My name is Monte Appel. I am a lawyer. My residence is St. Paul, Minn. I have offices also in Washington, and I appear here in support of Senate bill 4318, n behalf of the American stockholders of Synthetic Patents Co. who are affected by the bill.

It may be most helpful to the committee if I state the facts briefly of this one particular case which is affected by this bill. The facts of that particular case are as follows:

During the years 1912 to 1917, inclusive, the Synthetic Patents Co. was a corporation engaged in the manufacture and sale of pharmaceuticals.

The CHAIRMAN. Was this an American or foreign corporation?

Mr. APPEL. It was an American corporation organized under the laws of the State of New York, all of the stock of which was owned by three Germans who were citizens and residents of Germany during all of that period of six years from 1912 to 1917.

During the five years 1913 to 1917, inclusive, these three Germans received in Germany from this American corporation in America, under the terms of certain agreements which they made with the corporation, income in excess of $4,000,000, upon

which the income tax payable under the revenue laws of the United States amounted to $2,789,000, of which total tax $344,000 was the normal tax and $2,440,000 was the surtax.

In January, 1918, the Alien Property Custodian seized all of the stock of this company on the ground that the three Germans in Germany were alien enemies and that under the provisions of the Trading With the Enemy Act this stock, which was their property, was subject to seizure.

Senator WILLIAMS. How much did they pay under the income tax law?

Mr. APPEL. Nothing.

Then, after administering the property for a little more than a year, the Alien Property Custodian, in February, 1919, sold all this stock which he had seized from these Germans to American citizens, who had organized a corporation known as the Sterling Products Co. (Inc.), all of the stock of which they (the American citizens) owned, and the American citizens paid a little bit over $5,400,000 in cash for this stock and some other property.

Senator CALDER. To the Alien Property Custodian?

Mr. APPEL. Yes; to the Alien Property Custodian. Then, pursuant to the provisions of the trading with the enemy act, he deposited that $5,400,000 of proceeds from the sale with the Treasury of the United States, where it is now held subject to such disposition as Congress shall direct.

The three Germans to date have paid no income tax of any kind or nature upon this income in excess of $4,000,000 which they received from business carried on in the United States during the five years 1913 to 1917, inclusive.

After the Americans had bought the stock there was assessed against them and they were compelled to pay the normal tax in the amount of $344,000; and in order that you may understand the situation I should like permission for a minute to go into the provisions of the income tax laws in order to show how that came about.

The normal tax payable by nonresident aliens on income received from business which they conduct in the United States is required, under the provisions of the revenue laws, to be withheld and deducted here at the source.

The CHAIRMAN. Are you now speaking of the income of the individual or the income of the corporation? Is it the corporation tax or the individual tax?

Mr. APPEL. The individual tax; the tax which was leviable upon and payable by the three Germans, but which, as an administrative provision, in order to assure its collection, was required to be withheld and deducted at the source here. There was no provision requiring deduction and withholding at the source of the surtax by reason of the administrative impossibility of determining for each individual what the particular surtax was.

So that situation was one where so far as the surtaxes were concerned, there was no remedy at all against anybody on behalf of the Treasury, or against the Germans who were in Germany and who had removed all their property from the United States, except such as had been seized by and was in the custody of the Alien Property Custodian. But as to the normal tax, which was a relatively small proportion of the total tax, there was a secondary liability upon the corporation created by reason of the corporation's failure to deduct and withhold the normal tax out of the income transmitted to the Germans in Germany. But, of course, the Germans, having decided that they were going to pay no income tax, and owning all the stock of this corporation and controlling its actions, naturally saw to it that the corporation made no deduction and stopped no income at the source.

At the time of the sale of the stock to the Americans that then was the situation; the Germans owed an income tax of $2,789,000 to the Treasury of the United States.

A part of this total income tax—the normal tax of $344,000—had also become a secondary liability upon the corporation by reason of the corporation's failure to deduct and withhold during the period when the Germans owned all the stock of the corporation.

Senator WILLIAMS. The American purchasers took it with knowledge of the fact that they would have to pay that normal tax, did they not?

Mr. APPEL. The facts with reference to the knowledge of the Americans are set out in two affidavits, one by Mr. Frederick B. Lynch, who at that time was director and president of this company (the Synthetic Patents Co.), having been put there by the Alien Property Custodian as his representative to administer the business.

The other affidavit is by Mr. McClintock, who at that time was secretary and treasurer of the company, an appointee of the Alien Property Custodian.

It can also be stated, if it is considered material, that although Mr. Lynch has now no relation of any kind or nature with the company, Mr. McClintock was taken over by the Americans because he was so familiar with the details of the business and is still in the employ of the company.

Now, these two gentlemen in these affidavits which I will put into the record, but will not take the time to read now, have this to say:

DISTRICT OF COLUMBIA,
United States of America, ss:

Personally appeared before me, in the District aforesaid, this 4th day of November, A. D. 1922, Frederick B. Lynch, who being duly sworn deposes and says:

That on or about February, 1918, he was duly elected a director of Synthetic Patents Co., a corporation organized under the laws of the State of New York, and that on or about August 20, 1918, he was duly elected president of Synthetic Patents Co., and that he continued to be a director and president of Synthetic Patents Co. until on or about February 4, 1919, upon which date he tendered his resignation as director and president, which was duly accepted by the board of directors.

That during said period, when he was a director and president of Synthetic Patents Co., he performed such duties as are usually performed by a director and president of a corporation and became familiar with the business and affairs of Synthetic Patents Co.

That he learned that during the years 1913 to 1917, inclusive, all of the stock of Synthetic Patents Co. was owned by or for Rudolph Mann, Christian Hess, and Carl Duisberg, all of whom were citizens and residents of Germany; that he also learned that during the five years 1913 to 1917, inclusive, Synthetic Patents Co. had paid to Mann, Hess, and Duisberg sums of money aggregating in excess of $4,000,000, and that Mann, Hess, and Duisberg had never paid to the Government of the United States any income taxes upon the income so received; that he understood that some sort of a technical liability might be created against Synthetic Patents Co. to pay such taxes, but that this liability was only a contingent one and a remote one and would only become fixed in the event that the Government of the United States was unable to collect such taxes from Mann, Hess, and Duisberg, the three Germans who had received the income.

That later and along in the latter part of the year 1918 when the stock of Synthetic Patents Co., all of which had been owned by Mann, Hess, and Duisberg, and had been seized by the Alien Property Custodian as the property of enemy aliens, was being advertised for sale by the Alien Propery Custodian, he had occasion to look over the prospectus prepared by the Alien Property Custodian setting out the assets and liabilities of Synthetic Patents Co.; that this prospectus set out a very small estimated amount of money which might be due from Synthetic Patents Co. to the United States on account of taxes, which amount, as he remembers, was about $10,000; that while he did not know that any sum of money was actually owing by Synthetic Patents Co. to the Government of the United States on account of income taxes, he assumed that such sum in the amount of about $10,000 represented merely minor adjustments on income taxes, and having this thought in mind he considered the prospectus in this respect to be a substantially accurate statement of the tax liabilities of Synthetic Patents Co. to the Government of the United States; that while the stock of Synthetic Patents Co. was being advertised for sale by the Alien Property Custodian he had occasion from time to time to advise various prospective purchasers as to the nature and extent of the company's assets and liabilities, which action he considered to be in line with his duties as president of the company; that among other prospective purchasers he advised Sterling Products (Inc.), that the prospectus gotten out by the Alien Property Custodian was correct, which advice he believed to be true; that he also advised that there was some sort of a possible contingent liability which might fall back against the company if the Government of the United States was unable to secure payment of income taxes owing by the three Germans who had formerly owned all of the stock of the company, but that under the law as he understood it and as he was advised, the United States could collect such taxes owing by the three Germans out of the proceeds that would be paid to the United States by any purchaser of the stock, and that such action would undoubtedly be taken by the United States, and this possible contingent liability in the amount of about $350,000 would never become a fixed liability, and that the purchaser could go forward with their purchase, relying upon the correctness of the statements made in the prospectus of the Alien Property Custodian with reference to the assets and liabilities of Synthetic Patents Co.

FRED'K B. LYNCH.

Subscribed and sworn to before me this 4th day of November, 1922.

[SEAL.] RUTH C. ROWE, *Notary Public.*

STATE OF NEW YORK,
County of New York ss:

Earl I. McClintock, of the city, county, and State of New York, of lawful age, being duly sworn, deposes and says:

That on or about August 20, 1918, he was appointed secretary and treasurer of the Synthetic Patents Co. (Inc.) by the board of directors then controlling the policies of said company; that all of the members of said board of directors had been appointed by the Alien Property Custodian, who at that time was the holder of the entire capital stock of the company and who controlled and directed the company through the board of directors which he had appointed; that subsequently, and while serving as secretary and treasurer of the company, deponent became aware of the existence of the claim of the Bureau of Internal Revenue against the former German owners of the property, Rudolph Mann, Christian Hess, and Carl Duisberg, as individuals; that such income-tax liability was regarded by the company, and it had been so advised by counsel, as a primary liability against the three before-named Germans as individuals and only as a secondary liability against the company in the event the Government was unable to collect such taxes from the aforementioned Germans who had received the income on which such taxes were claimed to be due; that during the period of time when the stock of this company was being advertised for sale by the Alien Property Custodian, it was deponent's duty as secretary and treasurer of the company to advise such prospective purchasers as to the assets and liabilities of the company and he was frequently consulted by prospective purchasers; that he advised said prospective purchasers, among them Sterling Products (Inc.), the successful bidder, of the existence of the claim of the Bureau of Internal Revenue against the Germans; and he advised such prospective purchasers, among whom was Sterling Products (Inc.), the successful bidder, that said liability was undoubtedly primarily an obligation upon the former German owners as individuals and that he had no doubt the Alien Property Custodian would satisfy this obligation when he had funds in his possession with which to do so, and that no purchaser of such stock would be subjected to any liability on account of the failure of the Germans to pay income taxes on the income received by them.

E. I. MCCLINTOCK.

Subscribed and sworn to before me this 2d day of November, 1922.

EDW. J. HAUSER,
Notary Public, Bronx Coounty.

The CHAIRMAN. Was Mr. McClintock, if that was his name, an employee of the corporation while it was under German control?

Mr. APPEL. No; he was not an employee of the company while it was under German control, but after the Alien Property Custodian seized all of the stock, then, of course, he dismissed all of the directors and officers who had been there representing the Germans, and he put in his own representatives, among them Mr. Lynch, who became president, and Mr. McClintock, who became secretary-treasurer.

Mr. McClintock's first association with the company was under appointment by the Alien Property Custodian. When the Americans took the company over, they found it necessary to retain some one who knew the affairs of the company, and so retained Mr. McClintock. I do not know that it is material, but I did want to bring that to your attention.

These gentlemen say that after they took charge of the company they became familiar with its affairs; that they assisted in the preparation of the prospectus showing the assets and liabilities of the company, which prospectus was distributed to various prospective purchasers of the stock, and that notices were sent out that it was going to be put up for sale to the highest bidder; that they believed the statements contained in that prospectus to be correct; that, among other things, the prospectus stated that there was due to the United States an estimated amount of income tax of about nine or ten thousand dollars; that although they did not understand exactly what that meant, they assumed that it meant a minor adjustment of past income taxes; that they also, in the course of the performance of their duties, became aware that there was some sort of a contingent secondary liability upon the corporation by reason of the failure of the Germans to pay their income taxes and by reason of the corporation's failure, while under German control, to make the proper deductions; that they never considered that a real liability upon the corporation and they never assumed in the preparation of this prospectus that the corporation would ever be called upon to make payment on that secondary or assured liability, and so advised these Americans who made the highest bid which was accepted.

The CHAIRMAN. Why didn't they assume that?

Mr. APPEL. Because they went forward upon the assumption that the Germans having received the income were liable under the income-tax laws of the United States to pay the income tax and that when the purchasers made payment to the Alien Property Custodian and the Alien Property Custodian deposited that money in the very vaults of the Treasury, that the Treasury, having the money in hand, would immediately collect all the taxes that were due to the Treasury. Furthermore, as I will develop later, they knew that even if they were temporarily compelled to pay this tax, they had a right to be reimbursed by the Germans.

Senator CALDER. What is the name of this corporation?

Mr. APPEL. The Synthetic Patents Co.

Senator CALDER. What does it manufacture?

Mr. APPEL. Pharmaceutical preparations. They were also connected in a way with the Bayer Co., which makes aspirin.

Senator CALDER. Does this concern include all of the property of the Bayer Co.?

Mr. APPEL. No. The Bayer Co. is an entirely separate corporation.

Senator CALDER. How much did you say they paid?

Mr. APPEL. Five million four hundred thousand and some odd dollars.

Senator CALDER. This stock was disposed of at public auction to the highest bidder, was it?

Mr. APPEL. Yes.

Senator CALDER. What is the chief value of this concern—patents?

Mr. APPEL. The trade-marks——

Senator CALDER. Or formulas or buildings or factories?

Mr. APPEL. There were patents, factory buildings, formulas, and trade names of drugs which had been manufactured and sold by these Germans for many years and had acquired a value by reason of that fact. I am sorry I am not familiar with all the details of that, Senator, but I can get them for you.

Senator CALDER. What occurs to me is this: The Germans were paid very large profits over a short period of years, and $5,000,000 seems very low when you consider the enormous profits this concern was making. How do you know that this tax due was not taken into consideration when the property was purchased?

Mr. APPEL. So far as the price being low is concerned, I do not believe that is so, Senator. These properties were bought in 1919, at a time when, as you know, everything was high and before these people got into it and got themselves organized a slump came; and I know it to be the fact that they have regretted they did not wait a year to make the purchase and make it during the period of depression when they felt they could have bought the property for a great deal less than they actually paid for it. I will show later and I think I can show conclusively that Congress never intended and the Americans never expected to pay this tax.

Senator MCLEAN. What return are they making now on the purchase price?

Mr. APPEL. I am sorry, Senator, that I can not answer that question.

The CHAIRMAN. Is this the fact, that the Government received about $5,000,000 which went into the Treasury in payment of the sale of this stock of this corporation?

Mr. APPEL. Yes, sir.

The CHAIRMAN. This was stock owned by these German aliens?

Mr. APPEL. Yes, sir.

The CHAIRMAN. The Government had it in its possession, then, and it seems to me there was nothing in the world to prevent the Government offsetting the claim against any claim on the part of the original stockholders in Germany.

Mr. APPEL. That is true.

The CHAIRMAN. And the purchasers of the stock had the natural right to assume that if German money was in the hands of the Treasury Department they could collect the entire tax out of the money in the Treasury.

Mr. APPEL. And that was what was represented to them and what they believed, and as reasonable business men had a right to believe, would be done.

Senator JONES. Would that be the normal tax for the corporation itself? I understood you to say that this stock was sold as an asset of the corporation.

The CHAIRMAN. I do not understand that there was any question of a corporation tax.

Mr. APPEL. This case involves the normal tax on the individual income received by the three Germans.

The CHAIRMAN. This is an individual tax?

Mr. APPEL. It is an individual tax payable by the Germans on income which the Germans received.

Senator CALDER. Can you give us the names of the directors and officers of this new corporation and the names of the principal purchasers of the stock?

Mr. APPEL. Yes; I can do that and I shall be glad to get that information for you as soon as I leave.

Senator WILLIAMS. I wish you would enlighten me with regard to one question. What was it that prevented the Treasury of the United States from collecting this $340,000?

Mr. APPEL. I shall be very glad to answer that.

Senator WILLIAMS. It seems to me the Treasury could have proceeded to take it out of that money, the corporation being subject to liability, owing to the fact that it had not paid the deductions. There was money in the Treasury, so why couldn't the Treasury Department take that amount? I do not mean the surtax but the normal tax.

Mr. APPEL. Although the revenue laws provide that in the event of the failure of the nonresident alien to pay the normal tax that all his property shall be subject to distraint, yet it was construed that the obscure provision in the trading with the enemy act, which said that this property should be held subject to such disposition as Congress shall direct, nullified all of those provisions in the revenue acts and surrounded this property of the Germans with immunity from distraint or seizure, which prevented not only its attachment or garnishment by the Americans, but also precluded the Treasury of the United States from dipping into it and collecting the tax.

Senator WILLIAMS. For past due debts?

Mr. APPEL. Yes.

Senator GERRY. In other words, the Treasury of the United States could not even collect that amount from the profits accruing to the company while it held it?

Mr. APPEL. That is quite true.

Senator WILLIAMS. It seems to me that is a far-stretched meaning to put upon it, but I can see how they arrived at their conclusion.

Mr. APPEL. It has always seemed to me that Congress wanted this problem held in status quo until it had the opportunity to consider the big problem and to make a determination of policy, but it is also true that when that clause was inserted in the act during the war nobody contemplated this particular income-tax feature.

There is another angle to this situation, if I may have a few more minutes of your time, that I should like to get before the committee, and that is, assuming the secondary liability of the corporation by reason of the failure of the primary debtors in Germany to pay their taxes, the revenue laws of the United States created in favor of the corporation the right of reimbursement over against the nonresident alien, effectuating the intention of Congress, which runs all through the revenue laws that always the ultimate payment of taxes shall rest upon the recipient of the income.

Senator WILLIAMS. Provided it can be made up by reliable persons.

Mr. APPEL. In this case, if it had not happened to come around as the result of the war that this property, when it was seized by the Government of the United States, was surrounded with immunity, not only could the Treasury of the United States reimburse itself, but the Americans, having been subjected to liability, would and could have immediately attached and garnished all money or property of the Germans in the United States in order to reimburse themselves for the taxes which they had temporarily been compelled to pay for account of the Germans. But it so happened that with this property in the Treasury, not only the Americans, but even the Treasury itself could not do it. This matter was once brought into litigation in the United States district court in New York before his honor Judge Knox, and the learned judge, after reciting the facts here, summarized his conclusions on the moralities and equities of the situation as follows: He says:

"In each of the present suits plaintiff 'inadvertently' paid to Hess, Duisberg and Mann"——

The CHAIRMAN. Just a moment, please. Tell us about this suit so that we can understand it. Against whom was it brought, and for what purpose?

Mr. APPEL. This was a suit brought by the American corporation; that is, by the Synthetic Patents Co., after all its stock had been acquired by the Americans and the Americans had been compelled to pay the normal taxes. The purpose of this suit was to recover back those taxes, and was brought against the Alien Property Custodian and the Treasurer of the United States.

The CHAIRMAN. By the original corporation?

Mr. APPEL. Yes. You see, the corporate entity remains the same at all times, and although all the stock of the corporation in the meantime has passed from the Germans to the Americans that does not affect the existence and continuity of the corporate entity. So that in reality this is a suit by the Americans against the Alien Property Custodian and the Treasurer of the United States and the three Germans upon whom they secured service by publication, to recover back this $340,000 of normal taxes which the Americans had been compelled to pay on behalf of the Germans, and this is where we run into this technical legal and legislative difficulty.

The CHAIRMAN. Who was the defendant?

Mr. APPEL. The defendants were the Alien Property Custodian and the Treasurer of the United States and these three Germans who, of course, are not personally present in the United States, but upon whom service was secured by publication under the laws of the State of New York. This matter came up to the court on a preliminary motion with reference to jurisdiction with all the facts before it; and the judge, summarizing the facts, said:

"Plaintiff, a New York corporation, alleges that all of its outstanding capital stock was formerly owned by three citizens of Germany, who are the alien defendants—Hess, Duisberg, and Mann. After the outbreak of the war all the plaintiff's stock was seized by the Alien Property Custodian under the provisions of the trading with the enemy act as the property of the aliens named. Thereafter, on or about February 4, 1919, the stock was sold to Sterling Products (Inc.), a West Virginia corporation, the proceeds of sale going into the hands of the Treasurer of the United States.

"During the year 1913, and continuing up until the outbreak of the war with Germany, plaintiff and the enemy defendants were parties to a contract whereby it was obligated to pay Hess, Duisberg, and Mann 75 per cent of all moneys which it should receive from the right to use certain patents, formulas, processes, etc. There was outstanding also between said parties another contract whereby plaintiff (the corporation) was obligated to pay to said enemy defendants the sum of $1,000 each for any new patents or formulas emanating from said aliens and used or acquired by plaintiff. There was also an indebtedness of large amounts owed by plaintiff to the aliens upon which interest had to be paid.

"During the period between 1913 and April 6, 1917, plaintiff made large annual payments to the aliens upon account of the aforesaid obligations, but through 'inadvertence' failed to withhold therefrom amounts due the United States for income taxes in respect thereto.

"Subsequent to the acquisition of plaintiff's stock by Sterling Products (Inc.), a delinquent income tax return was filed by plaintiff with the Internal Revenue Department, and in due course plaintiff was required to pay to the Government the sum of $344,102.50, being the amount of taxes it had failed to withhold from Hess, Duisberg, and Mann.

"The sum received by the Alien Property Custodian upon the sale of plaintiff's stock exceeded the taxes so paid, which are now sought to be recovered. Upon June 26, 1919, a claim therefor was filed with the custodian, pursuant to section 9 of the trading with the enemy act, as amended, no application being made to the President for an order of payment. * * *

"In each of the present suits plaintiff 'inadvertently' paid to Hess, Duisberg, and Mann sums of money which, by virtue of the laws of the United States, it was under no obligation to pay, but which, on the contrary, it was specifically bound to turn over to the United States. Why, then, if jurisdiction exists over the persons or property of the aliens, should they be permitted to retain moneys to which they are not rightfully entitled? Certainly, from a moral standpoint the money should be returned to plaintiff, and in my judgment such return should be compelled by law."

That was the reaction that this case made upon this United States district judge as to its moral equities, but under the technical situation, which we believe was not contemplated or intended by Congress, there seems to be no real remedy under the law unless there is some new legislation.

The CHAIRMAN. The Secretary of the Treasury has written me concerning this matter.

Senator MCLEAN. What was the result of that case in the court?

Mr. APPEL. The matter is still pending before the court, but the judgment of the lawyers who are handling it, as the situation has developed, is that this provision in the trading with the enemy act, by the terms of which property is held subject to such disposition as Congress shall direct, makes any real remedy doubtful.

Senator WILLIAMS. So that, if I understand your point, the district court judge's decision was that this money should be returned to the corporation, but because of legal technicalities a decision to that effect would not be enforcible in a legal way at this time.

Mr. APPEL. He did not on this motion come out flatly and say that, Senator.

Senator WILLIAMS. What did he say?

Mr. APPEL. This came up on a motion of the defendant, I think—no; it was a plea; and then, on a subsequent motion to dismiss and overrule.

Senator MCLEAN. Was the question of jurisdiction involved?

Mr. APPEL. That was the attack.

Senator WILLIAMS. With regard to that particular motion he decided that there was a moral right, but that peculiar circumstances made it impossible to enforce it?

Mr. APPEL. That is the real point, Senator.

Senator McLEAN. It was not a question of jurisdiction? Did he decide he had no jurisdiction?

Mr. APPEL. He did not decide, Senator, that he had no jurisdiction. He decided he had jurisdiction to go on and hear the case, but he had intimated that if the Americans should secure judgment it would be unenforceable. The Americans now come to you and ask for legislation which will protect them.

Senator McLEAN. Are there other legal points involved in relation to this same question?

Mr. APPEL. I do not know of any.

The CHAIRMAN. If the witness will allow me right there, I want to insert a couple of paragraphs, possibly three, from a letter dated January 15, 1923, written by the Commissioner of Internal Revenue, to whom this bill had been referred by Secretary Mellon. I have written Secretary Mellon to secure his advice concerning this matter. Now, the Commissioner of Internal Revenue states:

"There are many cases which will be affected by the proposed bill, but I wish to state for you the facts in only one case, one which was considered personally by both the Solicitor of Internal Revenue and by me.

"In this case a domestic corporation purchased from the Alien Property Custodian all of the stock of another domestic corporation which stock had previously been owned by citizens of Germany. At the time of the purchase of the stock the purchaser was advised of the fact that the corporation was liable for additional income taxes for prior years and also for additional taxes on royalties paid by it to German citizens from which it had failed to withhold the income taxes as provided in the revenue laws. The Bureau of Internal Revenue after the purchase of the stock made demand upon and collected from the corporation several hundred thousand dollars representing the tax for which it was liable on account of failure to withhold from the payments of royalties made to the German citizens. Because of the complete change of ownership of the stock in this corporation the Bureau of Internal Revenue did not assess against it the penalty provided in the various revenue acts for its failure to withhold from these payments. After the payment of this tax the company filed a claim with the Alien Property Custodian to recover the amount so paid. This claim was rejected by the Alien Property Custodian. Suit was then instituted against the Alien Property Custodian and the Treasurer of the United States in which the company sought to recover the amount of tax paid by it out of the moneys of the German citizens taken over by the Alien Property Custodian. An answer has been filed to this suit by the Alien Property Custodian and the Treasurer of the United States setting up the fact that the company had failed to withhold the tax due from the aliens and further that the arrangement by which the money was paid to the aliens was for the purpose of avoiding the tax due the United States Government. A further defense was set up that the right of action, if any, on the part of the company arose after August 6, 1917, and consequently is not such a debt owned by an alien as is contemplated by the trading with the enemy act.

"The corporation subsequently requested that the bureau refund to it the tax that it had paid on account of its failure to withhold from the payment made to the German citizens and that the amount of such taxes be collected from the Alien Property Custodian. In a well considered opinion the Solicitor of Internal Revenue held that the tax had properly been collected from the domestic corporation and that it could not now be refunded to it; furthermore that the bureau had no authority to request or demand the payment by the Alien Property Custodian of the amount of the tax out of the funds in his hands of these German citizens. I personally considered the case and concluded in agreement with the opinion of the solicitor, that the company had no legal right nor, in view of the fact that its stock was purchased with knowledge of the tax liability of the company, any equitable claim for the refundment to it of the tax perviously paid on account of its failure to withhold from the amounts paid to the German citizens.

"This case, the facts of which are briefly stated above, is by no means the only one in the department which will be affected by the proposed bill, but it is the one with which I am most familiar. I am advised that in quite a few cases additional taxes have been assessed against corporations the stock of which prior to the time of the assessment of the tax had been purchased from the Alien Property Custodian. In all of these cases, of course, a refund of the amount of the tax so collected would, under the proposed bill, have to be made to the corporations and the amount thereof collected from the Alien Property Custodian out of the proceeds of the sale of the stock."

The CHAIRMAN. Have you any comments to make upon that?

Mr. APPEL. I would like to make this comment, Senator. The question of notice or lack of notice on the part of the Americans of the existence of this tax liability which rested primarily on the three Germans and secondarily on the corporation is entirely immaterial to both the law and the equities of this situation. Legally, the primary liability to pay these individual taxes levied against the Germans was upon the Germans who received the income. The corporation, by reason of the default of the Germans who at the time of their default owned and controlled the corporation in its entirety, was subjected to a secondary liability to pay the taxes which were primarily levied upon the three Germans. Under the words of the revenue acts and also under the ordinary rules of suretyship without reference to the words of the revenue acts, the corporation, having been subjected to this secondary liability, had a right of subrogation to secure reimbursement from the three Germans whose taxes the corporation had been called upon to pay. This right of the Americans was not affected directly or indirectly in any way by notice or lack of notice on their part and their notice or lack of notice did not affect the amount of their bid by so much as a single dollar because in the first place they believed that when the Treasury of the United States got into its possession over $5,000,000 of money belonging to these Germans, it would immediately collect out of these moneys the taxes which were owing by these Germans to the Treasury of the United States, and they did not anticipate and as reasonable business men could not be expected to anticipate that an obscure provision in the trading with the enemy act, which said that the property of enemy aliens should be held subject to such disposition "as Congress shall direct," would be construed to nullify the plain provisions of the revenue laws and to throw around the property of the Germans an immunity which prevented not only the Americans but even the Treasury of the United States itself from satisfying just obligations out of these moneys.

And furthermore, although the Americans believed that the Treasury would collect all taxes due the Treasury out of these moneys held by the Treasury and that they would never be called upon to make good this contingent, secondary liability, they also knew that if they ever were called upon to make good this secondary, contingent liability and to pay to the Treasury the taxes owing to the Treasury by the Germans on income received by the Germans, they had a right under the revenue laws of the United States and under the ordinary rules of suretyship to secure reimbursement from the Germans for the taxes paid for their account and that under the revenue laws of the United States all of the property of the Germans was subject to distraint and under the ordinary laws of the United States all of their property was subject to attachment and garnishment and they did not anticipate and as reasonable business men can not be held to have anticipated that all of this property of the Germans would be given a preference by the Congress of the United States which would put the Germans in a position better than the position of American citizens in similar circumstances and prevent American citizens from satisfying just claims out of these moneys. It would seem to me that this whole problem ought to be handled as an entirety and that all of the parties ought to be put in the same position as they would have been in if there had been no war and the Germans had not been declared enemy aliens. Surely the Germans should not profit by reason of the fact that the war made it necessary to declare them enemy aliens, and surely they should not by reason of that fact be released from just taxes which they should have paid on income received from business carried on in the United States. It is unconscionable that there should be worked out any solution of this problem which will completely and entirely release the Germans and it seems to me equally unconscionable that any solution should be worked out which will leave the Americans saddled permanently with a liability for taxes on income not a dollar of which they ever received. The two foregoing results can be happily accomplished by the passage of this bill which does not take a dollar of money out of the Treasury of the United States but which on the contrary will put millions of dollars into the Treasury of the United States and thus reduce in some small degree the amount of taxes payable by the citizens of the United States. This result under the law and the equities of the situation should be effectuated without reference to the notice or lack of notice on the part of the Americans at the time they purchased the stock. Such is the law and in my judgment such are the equities of this situation, and in support of my contention I would refer you again to the decision of United States District Judge Knox wherein the learned Judge summarized the material facts in this case and made no mention of the fact of notice or lack of notice on the part of the Americans and stated unequivocally that morally and equitably the ultimate liability for these taxes should be on the Germans and not on the Americans.

Senator WILLIAMS. It is simply a matter of transferring the money from one fund to another.

Mr. APPEL. Yes; that is what it does. It transfers it from a fund where the Treasury is holding it as trustee for the Germans into a fund to be used by the United States.

The CHAIRMAN. It is one of those cases where we are proceeding to obtain from the Government by law authority to obtain reimbursement of money that the corporation

has paid out for not withholding, prior to 1917, the moneys that were due for the tax which would be payable by the German stockholders for money earned in the United States.

Senator GERRY. Do I understand you to say that previous to the corporation's being taken over by the Alien Property Custodian it had earned profits of $4,000,000 in five years and that it was then sold by the Alien Property Custodian for $5,000,000 to American purchasers?

Mr. APPEL. Yes; $5,000,000.

Senator MCLEAN. Have you the names of these American purchasers?

Mr. APPEL. I sent and got a list of the directors and stockholders of this company. I can get that down here in a few minutes.

Senator MCLEAN. The Government appealed in the New York case?

Mr. APPEL. I am not sure.

Senator MCLEAN. You do not know, do you, whether there was a claim of collusion between the American purchasers and the former owners?

Mr. APPEL. There has never been the slightest suggestion of that kind, absolutely not a suggestion. There is not any question but that these American purchasers are high-class, honorable business men. There is not any question but that their bid was not only the highest bid, but that it was a high bid.

Senator SMOOT. What is the name of this company?

Mr. APPEL. The Synthetic Patents Co. It was the stock of the Synthetic Patents Co. which was purchased by the Sterling Products Co., which was a corporation organized by the American purchasers for that purpose.

Senator SMOOT. Have you a list of the stockholders of the American company?

Mr. APPEL. I have not, Senator, but I can get that for you.

Senator SMOOT. I should like to see a list of the stockholders.

The CHAIRMAN. I would like to call your attention to a paragraph in a letter of January 17 which the Secretary of the Treasury has written to me in response to my request or suggestion. He says:

"The proposed bill grants relief to citizens of the United States or domestic corporations who purchased the stock of corporations, which stock was formerly owned by alien enemies. It seems to apply with equal force to cases in which the purchaser of the stock had notice at the time of the purchase of the liability of the corporation for additional taxes to the Government of the United States, as well as the cases in which the purchase of the stock was made without notice of any liability for additional taxes to the Government. In those cases in which the purchaser was fully advised that additional tax was due the Government, this fact was, or should have been, a factor in determining the purchase price of the stock, and there seems to be, therefore, no equitable reason for granting the relief sought in such cases."

Mr. APPEL. If I may comment on that, Mr. Chairman, I would like to do so.

The CHAIRMAN. Yes.

Mr. APPEL. That would have force if applied to corporation taxes owing to the corporation, but it has no force, in my judgment, as applied to the secondary liability imposed by law upon the corporation for failure to withhold taxes on the income received by the Germans, for this reason, that it is the very essence of the revenue law that the recipient of the income shall pay the income tax; and the law as an administrative provision merely says that in order to assure collection of the normal tax we must impose upon the American corporation or upon anybody having and controlling funds in the American corporation the duty of deducting and withholding out of the income paid to a nonresident alien the normal taxes. Then, Congress, in order to effectuate its intention that always the ultimate payment shall be made by the recipient of the income, says that if the Americans controlling that income fail to pay it for any reason or fail to withhold or deduct it and they are compelled to pay, they shall immediately have the right of reimbursement from the nonresident alien.

The CHAIRMAN. I think it is quite clear that the real debt is owed by the German citizens and that the Government has the money, and, having the money to pay it, it ought not to enforce the secondary liability and at the same time relieve the persons primarily liable.

Senator SMOOT. If they have money that belongs to an individual himself, they ought first to take out what the individual owes.

Senator MCLEAN. It is a primary liability on the part of the corporation or on the part of the individual?

Senator SMOOT. Well, I know this, that if a corporation sells out and it is later discovered that there is an additional tax owing from that corporation, the purchasers of the new corporation are held liable.

The CHAIRMAN. This is not a corporation tax at all.

Senator SMOOT. I do not care whether it is a corporation tax or not. I say that in that case they are held liable.

The CHAIRMAN. It is a legal duty to withhold the normal tax. We levy a normal tax against the individual who earns the income or who receives the income. That is the original obligation.

Mr. APPEL. He is the original obligor.

The CHAIRMAN. To protect ourselves we hold that the corporation must withhold it.

Senator GERRY. It seems to me that this case is somewhat different, because the Germans, in order to evade the tax, insisted upon the corporation paying all the money over to them. Now, this property was sold and the profits from it are in the hands of the Government. The Government can now reimburse itself from that property which is really taking the stock from the German stockholders who were originally responsible. It is different from the case of an ordinary corporation.

Senator SMOOT. Let me call your attention to this. In that letter of January 17 the Secretary says, after the statement the chairman just read:

"Furthermore, even cases in which the purchasers were not advised of the additional tax which was pending at the time of the purchase of the stock do not differ from other cases, which frequently arise, where additional taxes are assessed against a corporation after there has been a change of ownership of a majority of its shares and for years prior to such change of ownership. I see no special reason for granting relief in the type of cases covered by the proposed bill and not granting relief in other cases in which additional taxes are assessed against a corporation, after a change of ownership of a majority of the shares of its stock, for years prior to such change of ownership. In all of these cases it would appear that the purchaser should have advised himself prior to the purchase of the stock of the status of the tax liability of the company and the mere fact that this matter was not considered prior to the purchase does not seem to me to be sufficient ground for granting relief."

The CHAIRMAN. Another reason is this, that the Government has in its hands the money of the debtor.

Senator SMOOT. I realize that.

The CHAIRMAN. And, having the cash in its hands, there is no reason that I can see why it should not say to the debtor in the final settlement, "We will withhold and will not return to you that portion which you owe the Government."

Senator SMOOT. I doubt very much whether they can do it. I do not think the Government can do it.

The CHAIRMAN. They can not under the law. That is the object of the bill, to give them that right.

Senator SMOOT. I have not read the bill. I have not had the opportunity.

Senator MCLEAN. I suggest that we hear what the witness has to say.

Mr. APPEL. I think I can clear that up. The law provides that—

"All persons, corporations * * * having control * * * of * * * income of any nonresident alien * * * are hereby authorized and required to deduct and withhold from such * * * income such sum as will be sufficient to pay the normal tax * * * ; and they are each hereby made personally liable for such tax * * *."

Now, this duty to stop at the source is merely an administrative duty. The tax is not thereby levied upon the withholding agent. On the contrary, the Treasury Department, in recent cases, citations of which I will give, has held that—

"Such taxes have never been considered as levied upon the one whose duty it is to pay the tax. In the case of domestic concerns required by the above-quoted provisions of the revenue act to withhold and to pay into the Treasury a certain percentage of the income of nonresident aliens and foreign corporations of which they have control, it is apparent that the tax is not levied upon the withholding agent, but is levied upon the income of nonresident aliens and is collected through with the withholding agent."

Senator MCLEAN. In this case, as I see it, you have a default of the parties originally and primarily responsible.

Mr. APPEL. Then the law is that by reason of the default of the persons primarily liable, the contingent liability of the withholding agent, which is in the nature of a surety liability, becomes a fixed liability, and the withholding agent is called upon to pay by reason of the default of the primary debtor. and then the withholding agent is given the right of reimbursement over against the primary debtor.

Let us assume that I want to borrow $100 from the bank. The bank does not know me and my credit is not good. I ask the Senator to indorse my note, which he does. The note thus indorsed is given to the bank and I get the $100. In 90 days it becomes due and I do not pay it. The Senator is called upon to pay. He goes to the bank and says, "Has Appel, in the meantime, put any money in the bank?" They say, "Yes; he put $500 in the bank." Then the Senator says, "Under the law you have the right to reimburse yourselves out of the moneys which you hold for Appel and you

should exhaust all your remedies against the maker of the note before you call on the surety. I ask you to take that money out of his deposits," which the bank would do, and therefore the surety would never be called upon to make good the note. Now, in this case, that was exactly what these Americans thought the Treasury was going to do and what the Treasury, if it had not been for this obscure provision, would have done, but in order to draw the analogy clear through, the bank in this case would say, "There has been a recent piece of legislation which precludes us from doing that, so although we have that money we can not touch it, so, Senator, you have to pay it because you indorsed the note." Then the Senator would come back and demand payment of me. If I did not pay he would sue me, and garnishee the money in that bank and thereby reimburse himself, and I, the person primarily liable, would be the person who would make the ultimate payment.

Senator SMOOT. Isn't that the proper way to do it?

Mr. APPEL. Yes, but the difficulty in this case is that there was inserted in the trading with the enemy act a provision which said that this property shall be held subject to such disposition as Congress shall direct and inadvertently, I believe, the property of these Germans was surrounded with immunity which prevents distraint proceedings and prevents any Americans from having recourse against it, so that that remedy can not be brought about, and what would be done in an ordinary case is precluded in this case.

Senator SMOOT. Do you think if this bill is passed it will work out all right?

Mr. APPEL. Yes, sir.

The CHAIRMAN. Mr. Miller, the Alien Property Custodian, is here. I should like to have him take the stand for a minute.

STATEMENT OF HON. THOMAS W. MILLER, ALIEN PROPERTY CUSTODIAN.

The CHAIRMAN. Mr. Miller, have you any suggestions which you wish to make with reference to Senate bill 4318?

Mr. MILLER. Mr. Chairman, this bill was forwarded to me from the Treasury Department originally, it having been referred to them by you as chairman of the Finance Committee. I am familiar with the details of this matter. I have been listening to this discussion to-day, and as there is very little left for me to say, I shall be very brief.

After the seizure of certain properties by the Alien Property Custodian, investigations were made by the income tax unit of the Treasury to determine what income taxes had accrued but had not been paid during the years prior to the seizure of the properties and while they were owned by enemy aliens. As a result of these investigations, the income tax unit discovered a large amount of such delinquent taxes, and, in certain cases where, at the same time the properties had been sold by the Alien Property Custodian to Americans, the Americans were compelled to pay these income taxes, both corporate and personal, on the income which had been received by the enemy aliens prior to the seizure by the Alien Property Custodian and prior to the date of acquisition of the properties by the Americans.

Now, gentlemen of the committee, I do not know whether you are asking for recommendations or not, but I am going to submit here a list of the corporations of which the Alien Property Custodian sold 40 per cent or more of the stock, showing the amounts and dates of additional taxes assessed, subsequent to date of sale of the stock, for 1917 and prior years.

List of corporations which the Alien Property Custodian sold 40 per cent or more of the stock, showing the amounts and dates of additional taxes assessed, subsequent to date of sale of the stock, for 1917 and prior years.

Name of company.	Year.	Additional tax.	Assessment list.
Alpha-Omega Publishing Co., Aeolian Hall, New York.	1917	None	None.
American Industrial Gas Co., 60 Wall Street, New York.	1917	do	Do.
American Junkers Co. (Inc.), 100 Broadway, New York.	1917	do	Do.
American Lava Co., Chattanooga, Tenn.	1917	$63.99	February, 1921.
American Metal Co., 61 Broadway, New York.	1909–1917	$122,792.97 overassessment.	
American Pyrophor Co., 317 East Thirty-fourth Street, New York.	1917	None	None.
American Radium Co., 7 East Forty-second Street, New York.	1917	do	Do.

List of corporations which the Alien Property Custodian sold 40 per cent or more of the stock, showing the amounts and dates of additional taxes assessed, subsequent to date of sale of the stock, for 1917 and prior years—Continued.

Name of company.	Year.	Additional tax.	Assessment list.
American Storage Co., 560 Broadway, New York.	1917	None	None.
Associated Operating Co., 8 Bridge Street, New York.	1917–1919	$8,285.32	To be assessed.
Atlantic Welding Corporation, 61 Broadway, New York.	1917	None	None.
Audiger & Meyer Silk Co., 130 Bond Street, New York.	1917	do	Do.
R. G. Barthold & Co. (Inc.), 72 Cliff Street, New York.	1919	$2,914.31	To be assessed.
Bauer Chemical Co., 30 Irving Place, New York.	1917	None	None.
Philipp Bauer Co., 2–4 Stone Street, New York	1915	$69.54	June, 1918.
	1916	$286.98	June, 1918.
Bayer Co. (Inc.), 117 Hudson Street, New York.	1913–1917	Purchasers advised of additional tax at sale.	
Beer, Sondeimer & Co. (Inc.), 61 Broadway, New York	1915	$261.36	May, 1918.
	1917	$86.60	April, 1921.
Ernst Gideon Bek (Inc.), 15 Maiden Lane, New York.	1917	$2,605.92	
Berger & Wirth (Inc.), 58 Columbia Heights, Brooklyn, N. Y.	1917	$821.43	June, 1920.
Blake Corporation, Derby, Conn	1917	None	None.
Bloch & Hirsch Fur Co., 24 Emerson Place, Brooklyn, N. Y.	1915–1919	do	Do.
Boonton Rubber Manufacturing Co., Boonton, N. J.	1911–1920	do	Do.
Bosch Magneto Co., 225 West Forty-sixth Street, New York.	1917	$10,640.13	To be assessed.
Bronze Powder Works Co., 801 Magnolia Avenue, Elizabeth, N. J.	1909–1917	$14,304.59	Paid by Alien Property Custodian.
Chillingworth Manufacturing Co., Carbon Place, Jersey City, N. J.	1917	$2,434.73	Claim filed by Lippett & Wood.
J. P. Devine Co., 1372 Clinton Street, Buffalo, N. Y.	1910–1918	$82.64	To be assessed.
Dresden Lace Works (Inc.), 30 East Twenty-first Street, New York.	1917	None	None.
Eisemann Magneto Co., 32 Bush Terminal Building, Brooklyn, N. Y.	1917	$12,835.23	To be assessed.
Heinr. Franck Sons (Inc.), Flushing, N. Y.	1910–1918	$910.97	1920.
Garfield Worsted Mills, Outwater Lane, Garfield, N. J.	1917	$4,226.21	September, 1920.
Emil Gebel Co., 193 West Street, New York City.	1917	None	None.
General Ceramics Co., 50 Church Street, New York.	1917	do	Do.
Gera Mills, Passaic, N. J.	1917	$283,525.44	To be assessed.
	1918	$412,675.30	Do.
C. P. Goerz American Optical Co., 317 East Thirty-fourth Street, New York.	1918	Overassessment, $678.80.	
Goetze Gasket & Packing Co., Allen Avenue, New Brunswick, N. J.	1917	$3,573.80	
Golde Patent Manufacturing Co. (Inc.), 509 West Fifty-sixth Street, New York.	1917	$1,867.73	
H. R. Heinicke (Inc.), 147 Fourth Avenue, New York.	1917–18	$1,957.70	To be assessed.
Chas. Hellmuth (Inc.), 154 West Eighteenth Street, New York.	1917	None	None.
J. A. Heenckels, 107 Chambers Street, New York.	1917	do	Do.
Heyden Chemical Works, 135 William Street, New York.	1917	do	Do.
Huntington Piano Co., Shelton, Conn	1917	do	Do.
International Textile (Inc.), Bridgeport, Conn.	1917	$77,322.71	May, 1920.
International Ultramarine Works (Ltd.), 113–115 Leonard Street, New York.	1917	$30,018.50	
Dr. Jaeger's Sanitary Woolen System Co., 395 Fourth Avenue, New York.	1918	$2,474.30	
Jagenberg Machine Co. (Inc.), 131 West Twenty-fourth Street, New York.	1917	None	None.
Kaffee Hag Corporation, 225 Fifth Avenue, New York.	1917	do	Do.
Kny-Scheerer Corporation, 404 West Twenty-seventh Street, New York.	1911	$338.52	February, 1919.
	1912	$306.38	Do.
	1913	$345	Do.
	1914	$15.48	February, 1920.
	1915–1917	None	None.

List of corporations which the Alien Property Custodian sold 40 per cent or more of the stock, showing the amounts and dates of additional taxes assessed, subsequent to date of sale of the stock, for 1917 and prior years—Continued.

Name of company.	Year.	Additional tax.	Assessment list.
Jacob & Josef Kohn (Inc.), 25 West Thirty-second Street, New York.	1917	$69.89	December, 1920.
La Salle Portland Cement Co., 140 South Dearborn Street, Chicago, Ill.	1918	None	None.
J. M. Lehmann Co., 101 Varick Street, New York.	1917	Overassessment, $130.50.	
E. Leitz (Inc.), 30 East Eighteenth Street, New York.	1917	None	Do.
Litosilo Co. of America (Inc.), 1011 Chestnut Street, Philadelphia, Pa.	1917	.....do	Do.
Locomotive Superheater Co., Wilmington, Del.	1917	.....do	Do.
H. Loeb & Co. (Inc.), 456 Fourth Avenue, New York.	1917	.....do	Do.
Markt & Hammacher Co., 193 West Street, New York.	1910–1916	$7,277.44	June, 1918.
Markt & Schaefer Co., 193 West Street, New York.	1910–1916	$2,358.89	
Merck & Co., 45 Park Place, New York.	1916	$1,813.81	May, 1922.
	1917	$79,284.98	March, 1920.
Messer Manufacturing Co., 121 North Seventh Street, Philadelphia, Pa.	1917	None	None.
New Brunswick Chemical Co., New Brunswick, N. J.	1917	$14,642.41	December, 1919.
New Jersey Worsted Spinning Co., Passaic Street, Garfield, N. J.	1909–1917	$23,852.95	
Norma Co. of America, 1790 Broadway, New York.	1917	$5,506.33	
North American Commodity Co., 112 Prince Street, New York.	1917	$1,050.61	May, 1920.
Pabst Brewing Co., 917 Chestnut Street, Milwaukee, Wis.	1917	None	None.
Pass-Washburn Co. (Inc.), 432 Fourth Avenue, New York.	1917	.....do	Do.
Pass-Kremer Hatband Co., 56 Mill Street, Paterson, N. J.	1914–1917	$1,843.70	September, 1919.
Passaic Worsted Spinning Co., Ninth Street, Passaic, N. J.	1917	None	None.
Perfection Furnace Pipe Co., Toledo, Ohio.	1917	$2,701.79	February, 1921.
Polack Tire & Rubber Co., 1876 Broadway, New York.	1917	None	None.
Frederick Pustet Co. (Inc.), Barclay Street, New York.	1917	Overassessment, $131.15.	
John Rath Cooperage Co., Chicago, Ill.	1917	None	Do.
Recreo Manufacturing Co., 417 Court, Utica, N. Y.	1917	.....do	Do.
Regine Shoe Co. (Inc.), 112 Prince Street, New York.	1917	.....do	Do.
G. Reis & Bros., 894 Broadway, New York.	1914–1917	$885.91	September, 1919.
F. ad. Richter Co. of New York, 74 Washington Street, New York.	1917	None	None.
Riedel & Co. (Inc.), 35 West Thirty-second Street, New York.	1917	$10.10	July, 1922.
	1918	$727.39	Do.
Rohm & Haas Co., 40 North Front Street, Philadelphia, Pa.	1917	None	None.
Ressie Velvet Co., 95 Madison Avenue, New York.	1917	.....do	Do.
Schaeffer & Budenberg Manufacturing Co., 338 Berry Street, Brooklyn, N. Y.	1917	$2,103.88	April, 1920.
Selas Co., 221 West Twenty-third Street, New York.	1917	None	None.
Senefelder Litho Stone Co. (Inc.), 32 Green Street, New York.	1917	.....do	Do.
G. Siegel Co., Chestnut Avenue, Rose Bank, Staten Island.	1917	.....do	Do.
Robert Soltau & Co. (Inc.), 158 West Twenty-third Street, New York.	1917	.....do	Do.
Sterling Co., Derby, Conn.	1917	.....do	Do.
Stollwerck Bros. (Inc.), Southfield Avenue, Stamford, Conn.	1917	$8,663.33	January, 1920.
Synthetic Patents Co. (Inc.), 117 Hudson Street, New York.	1913–1917	Purchasers advised of additional tax at sale.	
H. Tapke Realty Co., 52 Barclay Street, New York.	1917	None	None.
Topken Co., 257 Fourth Avenue, New York.	1917	$4,025.04	September, 1922.

List of corporations which the Alien Property Custodian sold 40 per cent or more of the stock, showing the amounts and dates of additional taxes assessed, subsequent to date of sale of the stock, for 1917 and prior years—Continued.

Name of company.	Year.	Additional tax.	Assessment list.
Traum Rubber Co., 239 Fourth Avenue, New York.	1917	None	None.
United Brush Manufactories, 203-205 Lafayette Street, New York.	1917	$16,874.46	
Vigilant Mills, 73 Leonard Street, New York.	1917	Overassessment $604.89.	
M. Welte & Sons (Inc.), 667 Fifth Avenue, New York.	1917	None	Do.
Werner & Pfleiderer Co., 1204 Niagara Street, Saginaw, Mich.	1917	.....do	Do.

I heard some one of your committee ask with reference to other cases that might be affected, and anticipating what might be in your minds I have gone into the matter and can state to you now that it involves several millions of dollars.

It is my position that the Alien Property Custodian occupies a position as trustee for the Government and trustee for the former holders of this property pending such time as Congress shall direct disposition of the property by the Alien Property Custodian.

As I understand it, it was said here to-day that this was merely a matter of taking this money, or some of this money, from one account of the Government and putting it into another account. I would be remiss in my duty as trustee if I did not call attention to the fact that these sums of money which have been realized from the sale of stock and which are now, under the law, being held by the Treasury subject to the Alien Property Custodian's orders are not, of course, in the same category with other public funds which the Treasury holds by reason of the collection of taxes, etc. We have been endeavoring to construe the law so that the Alien Property Custodian is a common law trustee.

If, after hearing all the facts in the case, our committee or Congress cares to take these sums of money out of the various trusts held by the Treasury for the Alien Property Custodian in order to reimburse the Commissioner of Internal Revenue, or direct reimbursement to be made in accordance with the terms of the bill, that is within your province.

I have read very carefully the letter of the Secretary of the Treasury, and in my opinion there should be some safeguards in this legislation as outlined in the letter. For instance, take a case where we have collected a certain amount of taxes and this law authorizes him to refund. The Alien Property Custodian's account in that particular trust might not be large enough to reimburse the Commissioner of Internal Revenue.

The CHAIRMAN. What about a case where stock is bought without a knowledge of the facts, as distinguished from a case where it is bought with knowledge of the fact that taxes are due?

Mr. MILLER. If it were shown in our contract of sale and in our advertisements of sale of these properties, of which the Synthetic Patents Co. is one, that the American purchasers knew full well that when they bought this property they were buying a tax liabillty from the Government, it might be well to differentiate that from the other case to which you have reference. If, on the other hand, they bought these properties without such knowledge, and then the income tax law of the Government came down on them and said, "This company, when it was operated by the Germans, owed a tax; they are beyond our reach; you bought this corporation, and we now expect you to pay this tax," then it is hard to expect the innocent purchaser to be made liable. But, while I have this opinion, still I consider myself the common law trustee, and I may add that I always scrutinize carefully any payments that I am asked to make and then make them, if they bear up under the scrutiny in accordance with the law.

Senator GERRY. I should like to ask the witness if the Alien Property Custodian construes the law so that any taxes that may have been due on any enemy aliens can not be paid from this fund that is held from the sale of these properties.

Mr. MILLER. The answer to that is written into the law, and very specifically so, in connection with the definition of debts that arose before the war. I am familiar, I may say, with this case, and it is impossible for me or my office or the Treasury Department to straighten this case out without additional legislation.

Senator GERRY. Then, as I understand it, if subsequently the properties, or funds derived from them, should be paid back to the original owners, unless additional legislation is passed they would get that amount without a reduction of the taxes?

Mr. MILLER. Yes.

The CHAIRMAN. Suppose you had not sold this property out and that the Alien Property Custodian still operated it. Under the law as it now stands you could deduct the taxes that are due from the debtor until Congress itself had provided for the disposition of the matter, could you not?

Mr. MILLER. No. I think a simple explanation will clear up that point. If we are operating as custodian, we hold that the custodian stands in the shoes of the majority of the stockholders, and the majority stockholders of the corporation to-day are paying their income taxes to the Government through the corporation.

The CHAIRMAN. That is not just what I mean. Of course, there is the amount which the corporation, by reason of its contingent liability, deducts. But these Germans owed a heavy surtax in addition to that, which debt they owed to the United States. The United States Treasury has their money, and yet you can not, under the law as it now stands, offset against their claim for the money which you received the amount of money due the United States until Congress has provided, under the law, for the disposition of that property.

Senator SMOOT. You are talking about surtaxes now, are you?

The CHAIRMAN. I am talking about surtaxes; yes.

Senator MCLEAN. Suppose the Alien Property Custodian does not have money enough to pay it from the collection of the normal tax?

The CHAIRMAN. Without a change in the law you can not even offset the debt of the Germans for the surtax.

Senator SMOOT. I do not know about that. It seems to me there is not any question about what the law means. Suppose that you should have a case of this kind: If all the taxes were paid, whenever the distribution of money is made to each individual stockholder, wouldn't the Alien Property Custodian insist upon——

Mr. MILLER (interposing). I have an arrangement, I may say, with the Commissioner of Internal Revenue that whenever I release my hold on property I first ascertain what taxes are due in the department from this trust, and they are paid before the final orders of release are given.

The CHAIRMAN. As I understand the matter, you have no way of disposing of a case of this kind unless you have additional legislation?

Mr. MILLER. Yes. There are, of course, a number of amendments to the law. I am not going into detail, but I can assure you that nothing is paid back to anyone unless I have found out first from the Commissioner of Internal Revenue what taxes are owing on his books.

I have in mind 23 big enemy insurance companies where they are getting ready to cut a fat melon in taxes. Because of my position, holding myself as trustee, I am bound to defend them.

The CHAIRMAN. Mr. Appel, you gave us an epitomized statement of certain affidavits. Do you want those affidavits printed?

Mr. APPEL. I have handed them to the reporter.

The CHAIRMAN. If there is no objection, we will have the affidavits printed as a part of your testimony.

Mr. APPEL. I have no objection.

Senator MCLEAN. Here is something which I should like to read. It is just a paragraph:

"The Alien Property Custodian has money and property belonging to the three Germans above mentioned. The bureau, however, can not demand payment by the Alien Property Custodian of the taxes due from Duisberg, Hess, and Mann, and even if the Alien Property Custodian were to make such payment, this office has no authority to refund to the corporation the taxes paid by it."

Mr. MILLER. We do need additional legislation.

The CHAIRMAN. As to the normal tax, the Government has already received it, and it can not do anything.

Senator SMOOT. I have not been thinking of the normal tax, but of the surtax.

Senator GERRY. As I understand it, this witness has said, in answer to my question, that he has not the authority to pay the taxes until further legislation is passed by Congress, because in legislation that had been passed there is a proviso that Congress would determine in the future what action should be taken.

Mr. MILLER. There is no way to pass on a case of this kind unless you have additional legislation.

Senator GERRY. Is there any legislation on the books that will take care of a surtax case?

Mr. MILLER. If there is any surtax due on an individual trust with the Alien Property Custodian and there is enough money to pay it, that money is paid by me or by my office before the claim is allowed. In this particular case, the Synthetic Patents case, you must have additional legislation. The money has already been collected by one branch, the internal-revenue branch. They can not come back and say the second time, "You pay it to us and when you pay it to us we will give it back to you."

Mr. APPEL. Perhaps I can help to clarify the situation.

There are now due from these three Germans to the Treasury of the United States surtaxes in the amount of $2,444,986.61. Those surtaxes have some of them been due to the Treasury of the United States since 1913 and others in successive years up to 1917. They have not yet been collected.

Senator SMOOT. They would not be collected until final settlement.

Senator GERRY. Can that final settlement be made without additional legislation?

Mr. MILLER. Yes: it can.

Senator SMOOT. That is the normal tax.

The CHAIRMAN. There is a question whether even that can be done.

Mr. APPEL. In my judgment, I fear the decision of the Treasury Department that they can not demand these taxes is correct under existing legislation. I think those moneys which are the proceeds of the sale of these properties and which are put into the Treasury of the United States subject to such disposition as Congress shall direct, are there under such terms as preclude any executive department or any individual from dipping into those funds and taking any out for taxes or anything else until the Congress does so direct.

Mr. MILLER. With due respect to the witness, I differ from him.

Senator MCLEAN. He bases his opinion upon the decision of the court.

Senator SMOOT. I agree with that as far as capital itself is concerned. I think that is true that far, but there is money from dividends.

Mr. MILLER. Yes.

Senator SMOOT. These dividends are paid into that company and then the surtaxes can be imposed, and you certainly will have enough money to pay them.

Senator MCLEAN. How about the other taxes?

Senator SMOOT. If he has money enough from the income on that capital, there is no doubt in my mind that the surtax has to be paid.

The CHAIRMAN. In the final settlement?

Senator SMOOT. Yes. I do not believe it can be done until final settlement.

The CHAIRMAN. We will have to look into the law. As I understand it, the law now reads that the property shall not be disposed of or interfered with until the final action of the Commissioner of Internal Revenue.

Mr. MILLER. I do not pretend to see any further ahead than the members of this committee. I think anybody can realize that the Alien Property Custodian stands in the shoes of the stockholders, and we are running a number of corporations which pay the income tax, the surtax, and other taxes in the usual course.

Senator GERRY. What about back taxes?

Mr. MILLER. With respect to that, I oppose an overassessment just as I would on my own taxes.

The CHAIRMAN. I suppose it is safe to say that the final disposition of that money has to be passed upon by Congress.

Mr. MILLER. Yes; that is the case under discussion. It seems to me a perfectly equitable proposition that we should enact legislation similar to this with the safeguarding changes suggested by the Secretary of the Treasury in his letter.

Senator SMOOT. I have not read this bill carefully because I have not had the time.

The CHAIRMAN. There are a number of amendments.

Senator SMOOT. All surtaxes can be paid at the time the final settlement is made.

The CHAIRMAN. There are other matters before the committee, and we shall now proceed to a consideration of them.

BRIEF SUBMITTED BY MR. MONTE APPEL.

The facts of one of the cases affected by S. 4318 are as follows:

1. During the years 1912 to 1917, inclusive, Synthetic Patents Co. was a corporation engaged in the manufacture and sale of pharmaceuticals.

2. During all of this period all of the stock of the corporation was owned by Christian Hess, Carl Duisberg, and Rudolph Mann, all of whom were and are now citizens and residents of Germany.

3. In the year 1912 Hess, Duisberg, and Mann licensed to the corporation certain patents which they owned in consideration of the payment to them by the corporation of certain royalties.

4. During the five years 1913 to 1917, inclusive, Hess, Duisberg, and Mann received from the corporation as royalties income in the amount of $4,361,242.65, all of which was taxable as income under the revenue laws of the United States, and upon which the normal income taxes payable to the United States amounted to $344,102.58 and the surtaxes amounted to $2,444,986.61, a total of $2,789,089.19.

5. In January, 1918, the Alien Property Custodian seized all of the stock of the corporation all of which was owned by Hess, Duisberg, and Mann, alien enemies.

6. In February, 1919, the Alien Property Custodian sold all of this stock to Sterling Products (Inc.), a corporation, all of the stock of which is owned by American citizens and pursuant to law deposited the proceeds of the sale with the Treasury of the United States.

7. Thereafter the corporation, all the stock of which in the interim has been acquired from the United States by American citizens, was required to pay and did pay to the Treasury of the United States the normal income taxes in the amount of $344,102.58.

8. The Treasury of the United States has not collected and under existing law can not collect the surtaxes in the amount of $2,789,089.19, owing to the Treasury by the three Germans who received the income upon which these income taxes are payable.

9. The three Germans who received from the United States income in the amount of $4,361,242.65 and who owe to the Treasury of the United States income taxes in the amount of $2,789,089.19 on account of the income so received have not paid to the United States any income taxes on this income of any kind or character.

10. The proceeds of the sale of the specific property of these three Germans which produced the income upon which the taxes are payable to the Treasury of the United States are being held in the Treasury of the United States subject to such disposition "as Congress shall direct."

The net result of the foregoing facts is that under existing legislation the Government of the United States can not collect the surtaxes in the amount of over $2,500,000 owing to it by three Germans in Germany who received from business carried on in the United States over $4,000,000 of income and can not refund to American citizens the normal income taxes in the amount of over $340,000 which it collected from these American citizens who never received any of the income, despite the fact that the Treasury of the United States holds over $5,000,000 of the money of these same three Germans derived from the sale of the specific property which produced the income which created the tax liability.

Obviously this inequitable result is the one not contemplated or intended by Congress and should be corrected by legislation.

The basic principle of the income tax is that it shall be paid by the recipient of the income. In this case the corporation composed entirely of American citizens has been compelled to pay the normal taxes of the nonresident aliens because section 9 (b) of the revenue act of 1916 as amended by the act of 1917 provides that "All persons, corporations * * * having control * * * of * * * income of any nonresident alien * * * are hereby authorized and required to deduct and withhold from such * * * income such sum as will be sufficient to pay the normal tax * * * ; and they are each hereby made personally liable for such tax * * *." This duty to so stop at the source, however, is merely an administrative duty. The tax is not thereby levied upon the withholding agent. On the contrary the Treasury Department has held that "Such taxes have never been considered as levied upon the one whose duty it is to pay the tax. In the case of domestic conerns required by the above-quoted provisions of the revenue act to withhold and pay into the Treasury a certain percentage of the income of nonresident aliens and foreign corporations of which they have control, it is apparent that the tax is not levied upon the withholding agent but is levied upon the income of the nonresident alien and is collected through the withholding agent." (Law Opinion 1107 of the solicitor of internal revenue, approved by the Commissioner of Internal Revenue, November 6, 1922.)

The income taxes, both normal and sur, upon the $4,000,000 of income received by the three enemy aliens were therefore due from three enemy aliens who had received the income. The corporation, which during all of the period of the payment of this income had been owned and controlled in its entirety by the same three enemy aliens, was subject to the penalty of being made to pay the normal taxes which these three enemy aliens had failed to pay and which they had precluded the corporation from withholding or paying.

At the time of the sale to the Americans of the stock of the corporation, the three enemy aliens owed to the Treasury of the United States $2,789,089.19 in taxes, of which $344,102.58 were normal taxes and $2,444,986.61 were surtaxes. The liability of the corporation itself was in the nature of a surety to pay the normal taxes. This liability on the part of the corporation was not a direct tax liability; on the contrary,

it was a secondary and contingent liability to make good the default of the primary debtors (the three enemy aliens) only if they themselves failed and refused to make good a liability which was on all grounds of law, equity, and justice theirs—and theirs alone, because if we look through the corporate device which these enemy aliens had rigged up, even the secondary liability upon the corporation was in substance at the time of its accrual the liability of the same three enemy aliens who owed all the stock and all the assets of the corporation. The sale of the stock of the corporation to the Americans did not release and was not intended to release the three enemy aliens from a single dollar of their tax liability to the Treasury of the United States. The Trading with the Enemy Act under which this stock was seized and sold was intended as a sword against and not as a shield for the enemy aliens.

The direct, primary liability for all income taxes, both normal and sur, on the $4,000,000 of income which they had received from the United States rested on the three enemy aliens at the time of the sale to the Americans and continued after the sale to rest upon them without release or modification of any kind or character. The Americans, therefore, by purchase of the stock did not assume this tax liability. They did not believe and, as reasonable business men, had no cause to believe that a direct, primary tax obligation against three enemy aliens for whose account the Treasury of the United States was about to receive and hold millions of dollars would be forever released while a secondary, contingent liability against the corporation whose stock they were buying would be permanently enforced. They knew that under the revenue laws of the United States the three enemy aliens, had they been American citizens, would be liable for and made to pay all income taxes due on the income received by them and that if they failed or refused to pay these taxes, all of their property would be distrained by the Government of the United States to effect collection of such taxes, and they believed and as reasonable business men had a right to believe that the same steps would be taken by the United States to effect or permit collection of moneys paid as taxes for enemy aliens as would be taken to enforce collection of taxes against American citizens. They knew that under the revenue laws of the United States, the failure of the three enemy aleins to return and pay these income taxes expressly subjected the property of such enemy aliens to the distraint of all of their property in the United States for the payment of such taxes, "and in case of his failure to file such return the collector shall collect the tax on such income, and all property belonging to such nonresident alien individual shall be liable to distraint for the tax" (sec. 6 (e) of the revenue act of 1916, as amended by the revenue act of 1917), and they believed and, as reasonable business men, had a right to believe that with the proceeds of the sale of the specific property of these particular three enemy aliens right in the vaults of the Treasury of the United States, collection of the taxes owing to the Treasury of the United States would be effected out of such proceeds which under the provisions of the revenue acts was made subject to distraint for taxes.

They did not anticipate and as reasonable business men had no reason to anticipate that these plain provisions of the revenue acts of the United States would be held to be nullified in their entirety by an obscure clause in the trading with the enemy act directing that enemy property should be held subject to such disposition as "Congress shall direct," and that such clause would be so construed as to impute to Congress an intention to create in favor of enemy aliens an immunity of their property from distraint for taxes while denying to American citizens all such immunity. And knowing these facts and believing in the plain words of the revenue acts, the Americans when they bought the stock of the corporation and paid to the United States millions of dollars for it, believed and had a right to believe, that the income taxes due on the income received by the three enemy aliens would be collected by the Treasury of the United States out of the millions which they, the Americans, were delivering into the custody of the Treasury of the United States and not out of the pockets of themselves who had never received a dollar of the income, and so knowing and believing, they, the Americans, saw no reason to reduce and did not reduce the amount offered and paid for the stock of the corporation.

And if by any chance the machinery of Government should work temporarily an enforcement of the secondary, contingent surety obligation of the corporation whose stock they were buying and they should be compelled to pay for the account of the three enemy aliens, income taxes on the income received by these enemy aliens, they knew that they were "indemnified against every person, corporation * * * or demand whatsoever for all payments they shall make" (sec. 9 (b) of the revenue act of 1916 as amended by the revenue act of 1917), and they knew such right of indemnification against the enemy aliens so created by the revenue laws of the United States placed the ultimate liability for the payment of these taxes upon the alien enemies and compelled the alien enemies to reimburse them, the Americans, for such taxes so paid

for their account. The amount of $344,102.58 is due from the enemy aliens as taxes levied upon them by the revenue laws of the United States and to-day exists unconditionally. It is not diminished or modified one iota by the knowledge or lack of knowledge on the part of the Americans at the time of their purchase of the stock of the failure of the three enemy aliens to discharge their just tax obligations to the United States and the consequent secondary, contingent liability of the corporation whose stock they were buying to pay the taxes owing by these aliens or their corporation to the United States if the Treasury failed to enforce collection against them. Congress intended unequivocally that the ultimate payment of income taxes should be made under all circumstances by the recipient of the income.

This case bears no relation to the ordinary case where additional taxes for prior years are assessed against a corporation after there had been a change of ownership of a majority of its shares, inasmuch as in the ordinary case recourse may always be had by the corporation against the primary obligor. The trading with the enemy act in this instance prevents both the Treasury Department and the withholding agent from collection and consequently there is no analogy between this case of withholding and the ordinary one.

This case can be best stated in the language of United States District Judge Knox when he summarized the material facts and moral equities of the case then before him as follows:

"The facts of the 'tax case' which was begun upon September 26, 1919, may be summarized as follows:

"Plaintiff, a New York corporation, alleges that all of its outstanding capital stock was formerly owned by three citizens of Germany, who are the alien defendants—Hess, Duisberg, and Mann. After the outbreak of the war all of plaintiff's stock was seized by the Alien Property Custodian under the provisions of the trading with the enemy act, as the property of the aliens named. Thereafter, upon or about February 4, 1919, the stock was sold to Sterling Products, (Inc.), a West Virginia corporation, the proceeds of sale going into the hands of the Treasurer of the United States.

"During the year 1913, and continuing up until the outbreak of the war with Germany, plaintiff and the enemy defendants were parties to a contract whereby it was obligated to pay Hess, Duisberg, and Mann, 75 per cent of all moneys which it should receive from the right to use certain patents, formulæ, processes, etc. There was outstanding also between the said parties another contract whereby plaintiff was obligated to pay to said enemy defendants, the sum of $1,000 each for any new patents or formulae emanating from said aliens, and used or acquired by plaintiff. There was also an indebtedness of large amount owned by plaintiff to the aliens upon which interest had to be paid.

"During the period between 1913 and April 6, 1917, plaintiff made large annual payments to the aliens upon account of the aforesaid obligations, but through 'inadvertence' failed to withold therefrom amounts due the United States for income taxes in respect thereto.

"Subsequent to the acquisition of plaintiff's stock by Sterling Products (Inc.), a delinquent income tax return was filed by plaintiff with the internal Revenue Department, and in due course plaintiff was required to pay to the Government the sum of $344,102.50, being the amount of taxes it had failed to withhold from Hess, Duisberg, and Mann.

"The sum received by the Alien Property Custodian upon the sale of plaintiff's stock exceeded the taxes so paid, which are now sought to be recovered. Upon June 26, 1919, a claim therefor was filed with the custodian, pursuant to section 9 of the trading with the enemy act, as amended, no application being made to the President for an order of payment.

* * * * * * *

"In each of the present suits plaintiff 'inadvertently' paid to Hess, Duisberg, and Mann sums of money which, by virtue of the laws of the United States, it was under no obligation to pay, but which, on the contrary, it was specifically bound to turn over to the United States. Why then, if jurisdiction exists over the persons or property of the aliens, should they be permitted to retain moneys to which they are not rightfully entitled? Certainly, from a moral standpoint, the money should be returned to plaintiff, and in my judgment, such return should be compelled by law."

The respective rights and liabilities of the parties under existing legislation are, therefore, as follows:

1. The Treasury of the United States is entitled to collect from the three nonresident aliens the surtaxes of over two and a half million dollars on the income in excess of $4,000,000 received by the three nonresident aliens, and

2. The Americans are entitled to be reimbursed the normal taxes of over $340,000 paid by them on the $4,000,000 of income received by the three nonresident aliens, and never paid by the aliens.

Congress at the time of the enactment of the trading with the enemy act could not foresee all the abnormal consequences which would flow from the economic disturbances brought about by the World War, and by an obscure provision inserted in the act for other purposes unintentionally precluded a rectification of the plain equities now existing. When Congress provided that the property seized from enemy aliens and the proceeds of the sale thereof should be held subject to such disposition "as Congress shall direct," Congress intended merely to keep the whole situation in statu quo until such time as it fixed the broad policy to be followed. Congress did not intend by this provision to preclude the collection by the Treasury of the United States of taxes from nonresident aliens, nor did Congress intend to nullify plain provisions of the revenue acts of the United States and surround the property of enemy aliens in this country with an immunity which would preclude the collection of taxes paid by American citizens for such enemy aliens. Congress, in fact, intended always that all income taxes owing to the Treasury should be collected by the Treasury and paid ultimately always by the recipients of the income. The problem here presented is solely a tax problem, and despite its ramifications is essentially one problem and should be treated as an entirety. S. 4318 provides for the collection of income taxes owing to the Treasury by the enemy aliens and for refundment to the Americans of the taxes which they were unjustly compelled to pay. It effectuates the expressed intention of Congress that ultimately always the recipient of income shall pay the tax. This bill if enacted into law will take no money out of the Treasury, but, on the contrary, will put large sums into the Treasury. It will, in the words of United States District Judge Knox, not permit the nonresident aliens "to retain moneys to which they are not rightfully entitled" and which "certainly, from a moral viewpoint, * * * should be returned to plaintiff (the Americans), and in my judgment such return should be compelled by law." This bill does not give to the Americans one dollar they are not entitled legally and morally to receive; it does not take from the nonresident aliens one dollar they are not obligated legally and morally to pay. It puts all parties in the exact position they would be in if they were all Americans dealing under the peace-time laws of the United States. It is fair and just to all parties and in accord with the highest principles of international dealing between the nations and private dealing between individuals. It is submitted that the bill should pass.

Respectfully submitted.

MONTE APPEL.

LETTER FROM THE SECRETARY OF THE TREASURY.

TREASURY DEPARTMENT,
Washington, January 17, 1923.

MY DEAR SENATOR: I have your letter of January 12, 1923, inclosing a copy of S. 4318, Authorizing the Secretary of the Treasury to make collections and refunds of taxes out of the proceeds of sales of roperty held in the Treasury, and requesting an expression of the Treasury's views thereon.

The proposed bill provides, in brief, that where citizens of the United States or a domestic corporation, all of the outstanding stock of which is owned by citizens of the United States, have purchased from the United States a majority of the outstanding shares of stock of a corporation, which shares of stock were formerly owned by persons who were or subsequently became alien enemies, and any additional taxes are found to be due from such corporation for the period prior to the purchase of its stock by American citizens or by a domestic corporation, the amount of such taxes shall be collected by the Secretary of the Treasury out of the proceeds of the sale of such shares of stock or other property which has been deposited in the Treasury of the United States. In cases where the tax has been assessed against and paid by the corporation since the purchase of its stock, the amount of additional tax so collected shall be refunded to the corporation and shall be then collected from the Alien Property Custodian out of the proceeds of the sale of the stock of the corporation or other property of the alien enemy which has been deposited in the Treasury of the United States.

In view of the fact that the property or the proceeds of the sale of the property out of which the amount of tax is to be collected by the Secretary of the Treasury are held under the provisions of the trading with the enemy act, this proposed bill is primarily a matter for consideration by the Alien Property Custodian and the Secretary of State, and it is suggested that it be referred to them for consideration before action is taken on it. There are certain features of the bill, however, which affect the Treasury Department and with which I am not in accord.

The proposed bill grants relief to citizens of the United States or domestic corporations who purchased the stock of corporations, which stock was formerly owned by

alien enemies. It seems to apply with equal force to cases in which the purchaser of the stock had notice at the time for the purchase of the liability of the corporation for additional taxes to the Government of the United States, as well as the cases in which the purchase of the stock was made without notice of any liability for additional taxes to the Government. In those cases in which the purchaser was fully advised that additional tax was due to the Government, this fact was, or should have been, a factor in determining the purchase price of the stock, and there seems to be, therefore, no equitable reason for granting the relief sought in such cases. Furthermore, even cases in which the purchasers were not advised of the additional tax which was pending at the time of the purchase of the stock do not differ from other cases, which frequently arise, where additional taxes are assessed against a corporation after there has been a change of ownership of a majority of its shares and for years prior to such change of ownership. I see no special reason for granting relief in the type of cases covered by the proposed bill and not granting relief in other cases in which additional taxes are assessed against a corporation, after a change of ownership of a majority of the shares of its stock, for years prior to such change of ownership. In all of these cases it would appear that the purchaser should have advised himself prior to the purchase of the stock of the status of the tax liability of the company and the mere fact that this matter was not considered prior to the purchase does not seem to me to be sufficient ground for granting relief.

The bill, moreover, should make some provision for those cases in which the statute of limitations has run against the collection of the amount of the taxes out of the proceeds of the sale of the stock. Furthermore, the bill makes no provision for cases in which the proceeds of the sale of the stock or the other property owned by alien enemies are insufficient to pay the entire tax, and it would be doubtful whether in such cases the bill authorized the collection of any deficiency from the corporation. Moreover, the provisions of the bill are indefinite with reference to the matter of refunding taxes theretofore paid by the person seeking relief, in that it does not provide that the taxes in question are not to be refunded until the Secretary has first collected such taxes out of the proceeds of the sale of such stock and other property on deposit in the Treasury. I think in protection to the Treasury Department there should be a specific provision that the tax shall not be refunded to the domestic corporation unless and until the amount thereof is collected out of the proceeds of the sale of the stock or other property.

I am inclosing for your information a copy of a memorandum from the Commissioner of Internal Revenue, dated January 15, 1923, as to the cases that have been settled by the Bureau of Internal Revenue or which are pending before it that will be affected by this bill.

Not wishing to make any recommendations with regard to the bill, I have set forth certain considerations which, in my opinion, are of significance in connection with the matter covered by the bill.

Very truly yours,

A. W. MELLON,
Secretary of the Treasury.

Hon. PORTER J. MCCUMBER,
United States Senate.

TREASURY DEPARTMENT,
BUREAU OF INTERNAL REVENUE,
Washington, January 15, 1923.

Memorandum for the Secretary.

At your request I have considered the bill S. 4318 and the effect that it will have upon cases that have been settled by the Bureau of Internal Revenue or which are pending before it.

The effect of the bill, briefly stated, is that in cases where persons have purchased a majority of the outstanding stock of a corporation, which stock was owned by persons who were or subsequently became enemy aliens, and any additional taxes are found to be due from such corporation that such taxes shall be collected by the department from the Alien Property Custodian out of the proceeds from the sale of the stock. In cases where the tax has been assessed against and paid by the corporation since the purchase of its stock the amount of the tax so collected shall be refunded to the corporation and shall then be collected from the Alien Property Custodian out of the proceeds of the sale of the stock of the corporation.

There are many cases which will be affected by the proposed bill, but I wish to state for you the facts in only one case, one which was considered personally by both the solicitor of internal revenue and by me.

In this case a domestic corporation purchased from the Alien Property Custodian all of the stock of another domestic corporation, which stock had previously been owned by citizens of Germany. At the time of the purchase of the stock the purchaser was advised of the fact that the corporation was liable for additional income taxes for prior years and also for additional taxes on royalties paid by it to German citizens from which it had failed to withhold the income taxes as provided in the revenue laws. The Bureau of Internal Revenue, after the purchase of the stock, made demand upon and collected from the corporation several hundred thousand dollars representing the tax for which it was liable on account of failure to withhold from the payments of royalties made to the German citizens. Because of the complete change of ownership of the stock in this corporation the Bureau of Internal Revenue did not assess against it the penalty provided in the various revenue acts for its failure to withhold from these payments. After the payment of this tax the company filed a claim with the Alien Property Custodian to recover the amount so paid. This claim was rejected by the Alien Property Custodian. Suit was then instituted against the Alien Property Custodian and the Treasurer of the United States, in which the company sought to recover the amount of tax paid by it out of the moneys of the German citizens taken over by the Alien Property Custodian. An answer has been filed to this suit by the Alien Property Custodian and the Treasurer of the United States setting up the fact that the company had failed to withhold the tax due from the aliens and further that the arrangement by which the money was paid to the aliens was for the purpose of avoiding the tax due the United States Government. A further defense was set up that the right of action, if any, on the part of the company, arose after August 6, 1917, and consequently is not such a debt owed by an alien as is contemplated by the trading with the enemy act.

The corporation subsequently requested that the bureau refund to it the tax that it had paid on account of its failure to withhold from the payments made to the German citizens and that the amount of such taxes be collected from the Alien Property Custodian. In a well-considered opinion the solicitor of internal revenue held that the tax had properly been collected from the domestic corporation and that it could not now be refunded to it; furthermore, that the bureau had no authority to request or demand the payment by the Alien Property Custodian of the amount of the tax out of the funds in his hands of these German citizens. I personally considered the case and concluded, in agreement with the opinion of the solicitor, that the company had no legal right nor, in view of the fact that its stock was purchased with knowledge of the tax liability of the company, any equitable claim for the refundment to it of the tax previously paid on account of its failure to withhold from the amounts paid to the German citizens.

This case, the facts of which are briefly stated above, is by no means the only one in the department which will be affected by the proposed bill, but it is the one with which I am most familiar. I am advised that in quite a few cases additional taxes have been assessed against corporations the stock of which prior to the time of the assessment of the tax had been purchased from the Alien Property Custodian. In all of these cases, of course, a refund of the amount of the tax so collected would, under the proposed bill, have to be made to the corporations and the amount thereof collected from the Alien Property Custodian out of the proceeds of the sale of the stock.

D. H. BLAIR, *Commissioner.*

(Thereupon, at 11.50 o'clock a. m., the committee proceeded to the consideration of other business.)

WSH # 22756

END OF
TITLE